

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION

AT RICHMOND, JULY 30, 2007

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APPLICATION OF

COLUMBIA GAS OF VIRGINIA, INC.

CASE NO. PUE-2007-00064

For approval to revise its tariff to allow the
implementation of an Off-System Sales
and Capacity Release Incentive Mechanism

APPLICATION OF

COLUMBIA GAS OF VIRGINIA, INC.

CASE NO. PUE-2007-00072

For approval of an amendment to a corporate
services agreement

ORDER FOR NOTICE AND COMMENT

On July 12, 2007, Columbia Gas of Virginia, Inc. ("Columbia" or "Company"), filed an application with the State Corporation Commission ("Commission") requesting authority to implement a proposed Off-System Sales and Capacity Release Incentive Mechanism ("Incentive Mechanism"). According to the Company's application, the implementation of the Incentive Mechanism will require: (i) revisions to the Company's Purchased Gas Adjustment ("PGA")/Actual Cost Adjustment ("ACA") mechanism in order to specify the manner in which off-system sales margins and capacity release revenue will be shared between customers and the Company under the Incentive Mechanism, and (ii) an amendment to the September 21, 2005 Service Agreement ("Service Agreement") between Columbia and NiSource Corporate Services Company ("NCSC") to clarify that the Service Agreement allows the off-system sales and capacity release transactions contemplated by the proposed Incentive Mechanism.

Under the Company's current PGA/ACA mechanism, all off-system sales margins and capacity release revenue are credited as an offset to gas costs through the Company's ACA. This treatment has the effect of giving customers 100% of the benefits resulting from off-system sales margins and capacity release revenue, thereby lowering customers' gas costs collected through the PGA/ACA mechanism. Based on the information contained in Attachment 3 to the Company's application, the off-system sales margins and capacity release revenue have benefited customers by crediting approximately \$1.8 million to \$4.5 million annually to the Company's gas costs during the 2002-2006 time frame.

The Company's application proposes to modify the traditional treatment of off-system sales margins and capacity release revenue in its PGA/ACA mechanism because of the Company's recent commitment to add significant new peak day capacity to serve customers. In the Company's recently concluded application for approval of a performance-based regulation plan ("PBR"), the Company committed itself to acquire significant additional peak-day capacity from its upstream suppliers and to undertake the distribution system enhancements necessary to make this new capacity available to customers.¹ According to the Company's application filed herein, the new capacity additions required under the Company's PBR plan will create additional opportunities for the Company to increase the value that can be generated by managing its gas supply assets in a manner that will benefit both customers and the Company. This additional value will be created, according to the Company, by expanding the supply management functions under the Company's current Service Agreement with NCSC to authorize such

¹ See *Application of Columbia Gas of Virginia, Inc., For approval of a performance based rate regulation methodology pursuant to Va. Code § 56-235.6*, Case No. PUE-2005-00098 and *Commonwealth of Virginia, ex rel. State Corporation Commission Ex Parte, In Re: Investigation of the justness and reasonableness of current rates, charges, and terms and conditions of service*, Case No. PUE-2005-00100, (Final Order, December 28, 2006). In addition to addressing issues relating to the acquisition of upstream capacity, the PBR freezes the Company's non-gas rates through December 31, 2010, and established an earnings sharing mechanism for non-gas revenues.

activities as flowing gas sales, incremental gas sales, physical gas options, exchanges, asset management arrangements and capacity release arrangements.

In order to provide an appropriate incentive to encourage the Company to maximize the value of its gas supply assets, the Company proposes to implement an Incentive Mechanism that will share off-system sales margins and capacity release revenue between customers and the Company. The proposed Incentive Mechanism has three components: First, in order to ensure that customers will preserve an appropriate level of benefits received from the current practice of crediting all off-system sales and capacity release revenues through the ACA, the Company proposes that 100% of the first \$2.5 million of off-system sales margins and capacity release revenue be credited to customers during the first year of the Incentive Mechanism, proposed to begin on November 1, 2007. This amount, according to the Company's application, is consistent with the historic level of ACA credits from off-system sales margins and capacity release revenue and is referred to as the "Program Year Threshold" in the application. In succeeding years, the Program Year Threshold will be adjusted each year in proportion to changes in the Company's firm capacity portfolio.²

Second, after the Program Year Threshold is met, the Company proposes that customers receive 35% and the Company receive 65% of all off-system sales margins and capacity release revenue until the amount received by the Company equals the Program Year Threshold. Finally, after Columbia receives an amount equal to the Program Year Threshold, the Company proposes that all amounts above that point be shared equally by customers and the Company.

² As explained in Attachment 1 to the Company's application, the Program Year Threshold of \$2,500,000 for the first year of the Incentive Mechanism will be adjusted each year by dividing the average Program Year peak day delivery portfolio for firm delivery into the Company's system for each month of the Program Year by 414,835 Dth (the Company's peak day firm delivery portfolio as of July 12, 2007), and multiplying the quotient by \$2,500,000. The product of the equation will be rounded to the nearest \$100,000. Attachment 4 of the application contains examples of how the Program Year Threshold will be calculated each year.

In order to implement the Incentive Mechanism, Columbia requests authority to revise its tariff pursuant to § 56-236 of the Code of Virginia ("Code"). The revised tariff provisions modify the PGA/ACA mechanism to define the scope of the Incentive Mechanism and to specify the manner in which off-system sales margins and capacity release revenue will be shared under the Incentive Mechanism proposed by the Company. The Company further proposes that the amended tariff provisions to implement the Incentive Mechanism become effective on November 1, 2007.

The Company further requests approval, pursuant to § 56-76 *et seq.* of the Code, to amend the September 21, 2005 Service Agreement between the Company and NCSC. The proposed revisions to the Service Agreement are designed to clarify NCSC's authority to perform the off-system sales and capacity release transactions contemplated by the proposed Incentive Mechanism.

NOW THE COMMISSION, upon consideration of the application, is of the opinion and finds that separate dockets should be established for reviewing the relief requested in the Company's application. The Company's application requests authority to amend the PGA/ACA mechanism in its tariff, which must be considered under Chapter 10 of Title 56 of the Code. The application also requests authority to amend the Company's Service Agreement with NCSC, which must be considered under the Chapter 4 of Title 56 of the Code ("Affiliated Interests Act"). The procedures adopted for investigating proposed changes to rate schedules filed under Chapter 10 differ considerably from the procedures used to evaluate applications filed under Chapter 4.

Section 56-237 of the Code requires the Commission to provide public notice and an opportunity for hearing before approving any changes in rate schedules on file with the

Commission.³ Applications filed under Chapter 4 are generally processed administratively by the Commission without notice or an opportunity for hearing.⁴

Section 56-77.A of the Code also requires the Commission to act on applications filed under Chapter 4 within a period of sixty (60) days, which may be extended for an additional thirty (30) days. The statute further provides that such an application "shall be deemed approved if the Commission fails to act within sixty days or an extended period ordered by the Commission." Applications filed under § 56-236 of Chapter 10 are not subject to such tight time constraints for the Commission to act on the application, nor does Chapter 10 contain any provision which deems applications approved "as a matter of law" if the Commission does not act within the statutory time frame.

Accordingly, given the different procedures used to evaluate applications filed under Chapter 10 and Chapter 4, we will establish separate dockets to consider the relief requested in the Company's application. We will evaluate the application to revise the Company's PGA/ACA mechanism in Case No. PUE-2007-00064. The Company will be directed to prefile testimony and exhibits in support of its proposed tariff revisions to its PGA/ACA mechanism and to provide public notice of its proposed tariff revisions. Interested parties will be given the opportunity to file comments and request a hearing on the proposed tariff revisions to the PGA/ACA mechanism that will be necessary to implement the proposed Incentive Mechanism. The proposed tariff revisions will also be suspended pursuant to § 56-238 of the Code, for one hundred fifty (150) days from the date the application was filed to and through December 9,

³ Section 56-40 of the Code allows the Commission to place into effect any proposed revision of rate schedules without notice when the proposed revision effects no increase in rates. However, the Company's application does not contain sufficient evidence to determine what effect the Incentive Mechanism will have on customers' rates.

⁴ See Va. Code §§ 56-77 and 56-84.

2007. We will establish Case No. PUE-2007-00072 to evaluate the Company's proposed changes to its Service Agreement with NCSC. The proposed amendment to the Company's Service Agreement with NCSC will be evaluated under the procedures used by the Commission to evaluate applications filed under Chapter 4 of Title 56 of the Code.

Accordingly, IT IS ORDERED THAT:

(1) The Company's application to amend its Service Agreement with NCSC and all associated papers, filed pursuant to Chapter 4, Title 56 of the Code, is docketed as Case No. PUE-2007-00072.

(2) The Staff shall investigate the proposed amendment to the Company's Service Agreement with NCSC and file an action brief with the Commission containing its findings and recommendations no later than sixty (60) days from the filing date of the application, or no later than ninety (90) days from the filing date of the application if the review period is extended by the Commission pursuant to § 56-77 of the Code.

(3) The Company's application to amend the PGA/ACA mechanism in its tariff and all associated papers, filed pursuant to Chapter 10, Title 56 of the Code, is docketed as Case No. PUE-2007-00064.

(4) In accordance with § 56-238 of the Code, the Company's proposed revisions to its PGA/ACA mechanism are hereby suspended for a period of one hundred fifty (150) days from the date the application was filed to and through December 9, 2007.

(5) On or before August 24, 2007, the Company shall file with the Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218-2118, an original and fifteen (15) copies of the testimony, exhibits, and other material supporting its application to revise the PGA/ACA mechanism in its tariff.

(6) A copy of the application and this Order shall be made available to interested persons who may obtain copies, at no charge, by making a request in writing to counsel to the Company, James S. Copenhaver, Columbia Gas of Virginia, Inc., 1809 Coyote Drive, Chester, Virginia 23836. Copies are also available for public inspection at the Commission's Document Control Center, Tyler Building, First Floor, 1300 East Main Street, Richmond, Virginia 23219, Monday through Friday, 8:15 a.m. to 5:00 p.m. Unofficial copies of the application and the Commission's Orders herein may be downloaded from the Commission's website:

<http://www.scc.virginia.gov/caseinfo.htm>.

(7) On or before August 24, 2007, the Company shall complete publication of the following notice to be published on one occasion as display advertising (not classified) in newspapers of general circulation within the service territory of Columbia:

NOTICE TO THE PUBLIC OF AN APPLICATION BY
COLUMBIA GAS OF VIRGINIA, INC., FOR AUTHORITY
TO AMEND ITS TARIFF IN ORDER TO IMPLEMENT
AN OFF-SYSTEM SALES AND CAPACITY
RELEASE INCENTIVE MECHANISM
CASE NO. PUE-2007-00064

On July 12, 2007, Columbia Gas of Virginia, Inc. ("Columbia" or "Company"), filed an application with the State Corporation Commission ("Commission") for authority to implement a proposed Off-system Sales and Capacity Release Incentive Mechanism ("Incentive Mechanism"). In order to implement the proposed Incentive Mechanism, the Company proposes revisions to the Purchased Gas Adjustment ("PGA")/Actual Cost Adjustment ("ACA") mechanism in its tariff in order to specify the manner in which off-system sales margins and capacity release revenue will be shared between customers and the Company.

Under the Company's current PGA/ACA mechanism, all off-system sales margins and capacity release revenue are credited as an offset to gas costs through the Company's ACA. This treatment has the effect of giving customers 100% of the benefits resulting from off-system sales margins and capacity release

revenue, thereby lowering customers' gas costs collected through the PGA/ACA mechanism.

The Company's application proposes to modify the traditional treatment of off-system sales margins and capacity release revenue because of the Company's recent commitment in Case No. PUE-2005-00098 to add new peak day capacity to serve customers. These new capacity additions, according to the Company, will create additional opportunities for the Company to increase the value that can be generated by managing its gas supply assets in a manner that will benefit both customers and the Company.

In order to provide an appropriate incentive to encourage the Company to maximize the value of its gas supply assets, the Company proposes to implement an Incentive Mechanism that will share off-system sales margins and capacity release revenue between customers and the Company. The proposed Incentive Mechanism has three components: First, in order to ensure that customers will preserve an appropriate level of benefits received from the current practice of crediting all off-system sales margins and capacity release revenue through the ACA, the Company proposes that 100% of the first \$2.5 million of off-system sales margins and capacity release revenue be credited to customers. This amount, according to the Company's application, is consistent with the historic level of ACA credits for off-system sales margins and capacity release revenue, and is referred to as the "Program Year Threshold" in the Company's application. In succeeding years, the Program Year Threshold will be adjusted each year in proportion with the changes in the Company's firm capacity portfolio. An explanation of how the Program Year Threshold will be adjusted after the first year of the program is contained in the Company's application.

Second, after the Program Year Threshold is met, the Company proposes that customers receive 35% and the Company receive 65% of all off-system sales margins and capacity release revenue until the amount received by the Company equals the Program Year Threshold, as calculated for each year of the program. Finally, after the Company receives an amount equal to the Program Year Threshold, the Company proposes that all amounts above that point be shared equally by customers and the Company. The Company proposed to implement the revisions to its PGA/ACA mechanism on November 1, 2007.

Pursuant to § 56-238 of the Code of Virginia, the Commission suspended the proposed tariff revisions to the Company's PGA/ACA mechanism to and through December 9, 2007. A copy of the Company's application and the Commission's procedural Order in this proceeding are available, at no charge, by making a request in writing to counsel for the Company, James S. Copenhaver, Columbia Gas of Virginia, Inc., 1809 Coyote Drive, Chester, Virginia 23836. Copies are also available for public inspection at the Commission's Document Control Center, Tyler Building, First Floor, 1300 East Main Street, Richmond, Virginia 23219, Monday through Friday, 8:15 a.m. to 5:00 p.m. Unofficial copies of Columbia's application and the procedural order in this proceeding may be downloaded from the Commission's website: <http://www.virginia.gov/caseinfo.htm>.

On or before September 14, 2007, any interested person may submit written comments or requests for hearing on the Company's application proposing tariff revisions to its PGA/ACA mechanism necessary to implement the Incentive Mechanism. An original and fifteen (15) copies of all such written comments and requests for hearing must be filed with Joel H. Peck, Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218-2118. Any request for hearing shall state with specificity why the issues raised in the request for hearing cannot be adequately addressed in written comments. If no sufficient request for hearing is received, the Commission may consider the application based on the papers filed without convening a hearing at which oral testimony is received. Persons filing a request for hearing and expecting to participate as a respondent in any hearing that may be scheduled shall also file, on or before September 14, 2007, an original and fifteen (15) copies of a notice of participation with the Clerk, State Corporation Commission, as required by 5 VAC 5-20-80 B of the Commission's Rules of Practice and Procedure, 5 VAC 5-20-10 *et seq.* Interested persons should refer to the Commission's Order for Notice and Comment for more information on participation as a respondent.

Interested persons desiring to submit comments electronically may do so on or before September 14, 2007, by following the instructions available at the Commission's website: <http://www.scc.virginia.gov/caseinfo.htm>.

Interested persons shall refer in their comments, requests for hearing, and notices of participation to Case No. PUE-2007-00064 and shall serve a copy upon counsel for the Company at the address set forth above.

Interested persons should consult the Commission's Order for Notice and Comment for further details regarding participation in this proceeding. Unofficial copies of the Company's application, the Commission's Orders entered in this proceeding, the Commission's Rules of Practice and Procedure, as well as other information concerning the Commission and the statutes it administers, may be accessed through the Commission's Document Search Portal at <http://www.scc.virginia.gov/caseinfo.htm>.

COLUMBIA GAS OF VIRGINIA, INC.

(8) On or before August 24, 2007, Columbia shall serve a copy of this Order on the chairman of the board of supervisors and the county attorney of each county and the mayor or manager of every city and town (or equivalent officials in counties, cities, and towns having alternate forms of government) in which the Company offers service. Service shall be made by first-class mail or personal delivery to the customary place of business or to the residence of the person served.

(9) On or before August 31, 2007, Columbia shall file with the Clerk of the Commission proof of notice and service as required herein.

(10) On or before September 14, 2007, any interested persons may submit written comments or requests for hearing on the application to revise the Company's PGA/ACA mechanism by filing an original and fifteen (15) copies of such comments or requests with the Clerk of the State Corporation Commission at the address set forth in Ordering Paragraph (5) above. Any request for hearing shall state with specificity why the issues raised in the request for hearing cannot be adequately addressed in written comments. If no sufficient request for hearing is received, the Commission may consider the proposed tariff changes based upon the papers filed herein without convening a hearing at which oral testimony is received. Interested persons shall refer in their comments or requests for hearing to Case No. PUE-2007-00064 and

shall serve a copy upon counsel for Columbia at the address set forth in Ordering Paragraph (6) above.

(11) Interested persons desiring to submit comments electronically may do so on or before September 14, 2007, by following the instructions available at the Commission's website: <http://www.scc.virginia.gov/caseinfo.htm>.

(12) On or before September 14, 2007, any person filing a request for hearing and expecting to participate as a respondent in any hearing that may be scheduled in this matter shall file an original and fifteen (15) copies of a notice of participation as required by 5 VAC 5-20-10 *et seq.* All notices of participation shall be filed with the Clerk of the State Corporation Commission at the address set forth in Ordering Paragraph (5) above. Copies of any notice of participation shall refer to Case No. PUE-2007-00064 and shall simultaneously be served on counsel for the Company at the address set forth in Ordering Paragraph (6) above.

(13) On or before September 21, 2007, the Staff shall investigate the proposed revisions to the PGA/ACA mechanism in the Company's tariff and present its findings and recommendations in a report, or testimony if appropriate, filed with the Clerk of the Commission and shall send a copy to counsel for Columbia and each respondent.

(14) On or before September 28, 2007, Columbia shall file with the Clerk of the Commission at the address set forth in Ordering Paragraph (5) above an original and fifteen (15) copies of any response, or testimony if appropriate, the Company expects to introduce in rebuttal. The Company shall also serve a copy of such response or rebuttal testimony upon the Staff and each respondent.

(15) Columbia and each respondent shall respond to interrogatories and other data requests within seven (7) calendar days after receipt of the same. Except as modified above,

discovery shall be in accordance with Part IV of the Commission's Rules of Practice and Procedure.

ATTESTED COPIES hereof shall be sent by the Clerk of the Commission to:
James C. Copenhaver, Columbia Gas of Virginia, Inc., 1809 Coyote Drive, Chester, Virginia 23836; C. Meade Browder, Jr., Senior Assistant Attorney General, Division of Consumer Counsel, Office of the Attorney General, 900 East Main Street, Second Floor, Richmond, Virginia 23219; and the Commission's Office of General Counsel and Divisions of Energy Regulation, Public Utility Accounting, and Economics and Finance.